

**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF COLORADO
Honorable Sidney B. Brooks**

In re:)	
)	
VALLEY MORTGAGE, INC.)	Bankruptcy Case No. 10-19101-SBB
)	Chapter 11
Debtor.)	
_____)	
)	
VMI Liquidating Trust Dated December 16, 2011))	
)	
Plaintiff,)	Adv. Proc. No. 12-01277-SBB
)	
v.)	
)	
UNITED STATES OF AMERICA, on behalf of))	
the INTERNAL REVENUE SERVICE,)	
)	
Defendant.)	
_____)	

**ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT’S MOTION FOR
SUMMARY JUDGMENT**

THIS MATTER is before the Court on the Defendant’s Motion for Summary Judgment and the Plaintiff’s Response thereto. For the reasons set forth herein, the Court GRANTS IN PART AND DENIES IN PART the Defendant’s Motion for Summary Judgment.

I. BACKGROUND AND FACTS

The case at hand is largely centered on the Debtor’s involvement in a Ponzi scheme and the use of the Debtor’s funds to pay the personal tax liability of the perpetrator of this Ponzi scheme, Mr. Phillip R. Lochmiller (“Lochmiller”).

Lochmiller was the majority owner and President of the Debtor. From February 2005 through July 2007, Lochmiller wrote eight checks to the Internal Revenue Service to pay his personal tax liabilities. Each of these eight checks was drawn on the general account of the Debtor and paid to the order of the United States Treasury. The checks totaled \$161,341.40.¹

¹ Copies of the individual checks are included in Exhibit #1 to the Defendant’s Motion for Summary Judgment (Docket No. 11). The date and amount of each check are as follows: (1) February 2005 for \$339.10, (2) April 2005 for \$6,758.00, (3) April 2005 for \$6,192.00, (4) March 2006 for \$3,227.54, (5) April 2007 for \$114,424.48, (6) June 2007 for \$15,800.00, (7) July 2007 for \$6,447.13, and (8) July 2007 for \$8330.15.

Lochmiller used the Debtor to perpetrate this Ponzi scheme until May 29, 2009 when the fraud was exposed and state court receivership proceedings commenced. A receiver was appointed and in April 2010, a Colorado state court expanded the receiver's powers to include the power to file for bankruptcy. Shortly thereafter, on April 19, 2010, the Debtor filed its petition for Chapter 11 bankruptcy. Exactly two years later, on April 19, 2012, the Debtor filed its Complaint, initiating the case at bar. In its Complaint, the Debtor alleges that the checks Lochmiller authorized for payment of his personal tax liabilities constitute fraudulent transfers. The Debtor seeks to recover the total of these eight checks – \$161,341.40 – pursuant to sections 548 and 544 of the United States Bankruptcy Code.²

In response to the Debtor's Complaint, the I.R.S. has filed an Answer and a Motion for Summary Judgment. In support of its Motion, the Defendant argues that the Debtor's claims are untimely, barred by the doctrine of sovereign immunity, and preempted by section 7422 of the Internal Revenue Code. In the event the Debtor's claims are allowed by this Court, the Defendant seeks summary judgment on the grounds that it took the transfers at issue in good faith, for reasonably equivalent value, and as a subsequent transferee.

II. SUMMARY JUDGMENT STANDARD

Summary judgment is appropriate if the pleadings, depositions, answers to interrogatories, admissions, or affidavits show that there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law.³ The moving party bears the initial burden of making a prima facie demonstration of the absence of a genuine issue of material fact and entitlement to judgment as a matter of law.⁴ In applying this standard, this Court examines the factual record and reasonable inferences therefrom in light most favorable to the non-moving party.⁵

III. ANALYSIS

a. The Plaintiff's Claim under Section 548 of the Code Is Dismissed.

The Plaintiff's first claim for relief, as asserted in paragraph 45 of its Complaint, seeks, in part, recovery of fraudulent transfers made to the Defendant under section 548 of the Code. In its Motion for Summary Judgment, the Defendant argues that the alleged fraudulent transfers are time-barred by the two-year statute of limitations contained within section 548 and, thus, should be dismissed. In response to the Defendant's argument, the Plaintiff asserted that it "does not allege any claim under [section 548 of the Code]." Regardless of whether the Plaintiff has or has

² Hereinafter, unless specified otherwise, all statutory references shall be the Title 11 of the United States Code.

³ FED.R.CIV.P. 56(d) made applicable to adversary proceedings by FED.R.BANKR.P. 7056.

⁴ *Whitesel v. Sengenberger*, 222 F.3d 861, 867 (10th Cir. 2000).

⁵ *Schwartz v. Bhd. of Maint. of Way Employees*, 264 F.3d 1181, 1183 (10th Cir. 2001).

not asserted a claim under section 548, such claim would be and is time-barred by the statute of limitations.

Under section 548, the trustee may avoid any fraudulent transfer made by the debtor within two years of the date of the debtor's bankruptcy petition. Here, the Debtor filed for bankruptcy on April 19, 2010. The last transfer in question to the Defendant occurred in July of 2007. Thus, all of the alleged fraudulent transfers to the Defendant occurred more than two years prior to the Debtor's bankruptcy petition and are therefore outside of the statute of limitations. Consequently, any claim the Plaintiff may have asserted under section 548 is untimely and, therefore, dismissed.

b. The Plaintiff's Claim under Section 544 of the Code and the Colorado Uniform Fraudulent Transfer Act (CUFTA) Is Timely

Section 544 of the Code contains what are commonly referred to as the trustee's strong-arm powers. As detailed in this section of the Code, those powers include the ability "to avoid any transfer of an interest of the debtor in property... that is avoidable under applicable law[.]"⁶ Generally, "applicable law" is interpreted to include state law causes of action, such as here where the Debtor's claim for relief is predicated upon the Colorado Uniform Fraudulent Transfer Act (CUFTA).⁷

Under CUFTA, a transfer is fraudulent if the debtor made the transfer:

- (a) With actual intent to hinder, delay, or defraud any creditor of the debtor; or
- (b) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor;
 - (I) Was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
 - (II) Intended to incur, or believed or reasonably should have believed that he would incur, debts beyond his ability to pay as they became due.⁸

The Debtor bases its theory of recovery on both section (a), which addresses claims for actual fraud, and section (b), which addresses claims for constructive fraud. Under both theories of fraud, a claim is timely if the claim is brought within four years after the transfer. However, unlike claims for constructive fraud under section (b), a plaintiff may bring a claim for actual

⁶ 11 U.S.C. § 544(b)(1).

⁷ *Sender v. Simon*, 84 F.3d 1299, 1304 (10th Cir. 1996) ("The trustee's powers under the section are predicated on non-bankruptcy law, usually state law, applicable to the transaction sought to be avoided."); 5 Collier on Bankruptcy ¶ 544.06[2] n.18 (Alan N. Resnick & Henry J. Somme eds., 16th ed.).

⁸ C.R.S.A. § 38-8-105.

fraud under section (a) more than four years after the transfer if the claimant did not or could not have reasonably discovered the fraudulent transfer during those four years. In such cases, the claimant has one year after the transfer was or could have been discovered to bring the claim.⁹

Under section 546 of the Code, the statute of limitations for state law actions brought under section 544 may be extended for a period of time. Where a statute of limitations for a state law action has not run before the debtor files for bankruptcy, section 546 provides the trustee in bankruptcy with some additional time to determine which actions, predicated on state law, he or she would like to bring on behalf of the debtor. “Without this [breathing spell], a trustee who does not immediately determine what potential claims are available for the recovery of assets may forever be barred from asserting those claims if the statute of limitations expires early in the bankruptcy[.]”¹⁰

Under Section 546(a)(1), “An action under section 544 may not be commenced after... the later of:¹¹

(A) 2 years after the entry of the order for relief; or

(B) 1 year after the appointment.. of the first trustee[.]^{12,,}

Reading both CUFTA and section 546 in conjunction, the debtor may bring a CUFTA action under section 544 of the Code within two years following the debtor’s bankruptcy petition so long as CUFTA’s four-year statute of limitations has not run prior to the filing of the debtor’s bankruptcy petition.

Here, the Debtor complied with the limitation stated in section 546 by filing its Complaint exactly two years following the filing of its bankruptcy petition. Therefore, the Debtor may timely attempt to recover alleged fraudulent transfers under CUFTA.

Under CUFTA, the Debtor has alleged causes of action based on constructive fraud and actual fraud. According to CUFTA’s statute of limitations, a debtor may seek to recover any fraudulent transfer, whether constructively or actually fraudulent, which occurred less than four years prior to the filing of the Debtor’s bankruptcy petition. Since the Debtor filed for bankruptcy on April 19, 2010, four years prior is April 19, 2006. Thus, the Debtor may attempt to recover any alleged fraudulent transfer which occurred on or after April 19, 2006. The Court deems such recovery efforts to be within the statute of limitations and declines to grant summary judgment in favor of the Defendant for any alleged fraudulent transfers which occurred on or after April 19, 2006.

⁹ C.R.S.A. § 38-8-110.

¹⁰ *In re Dry Wall Supply, Inc.*, 111 B.R. 993, 937 (D.Colo. 1990).

¹¹ An analysis under § 546(a)(2) is inapplicable because the case has not been closed or dismissed; thus, (a)(1) is “earlier” than (a)(2), and, thus, applicable to the facts at hand.

¹² 11 U.S.C. § 546(a)(1).

Further, as stated above, in cases of actual fraud, CUFTA allows a debtor to bring a fraudulent transfer claim more than four years after the transfer if the debtor did not or could not have reasonably discovered the transfer during those four years. In such cases, the debtor has one year after the transfer was or could have been discovered to bring the claim.¹³ A debtor's ability to discover a fraudulent transfer is a question of fact and, at this stage of the present case, the Court does not have enough information to determine that fact in favor of the Defendant. Therefore, the Court declines to grant summary judgment in favor of the Defendant for any alleged fraudulent transfers, conveyed with actual fraudulent intent, which occurred prior to April 19, 2006.

c. The Plaintiff's Claim under Section 544 Is Not Barred by Sovereign Immunity

Section 106 of the Code abrogates a governmental unit's sovereign immunity with respect to fifty-nine enumerated sections of the Code, including section 544.¹⁴ As explained above, section 544 contains what are commonly referred to as the trustee's strong-arm powers.

Germane to this case is a particular subsection of section 544 which allows the trustee to step into the shoes of an unsecured creditor, which, under non-bankruptcy state law, could have brought an action for recovery of a fraudulent transfer pre-petition. Specifically, under section 544(b)(2)(1):

[T]he trustee may avoid any transfer of an interest of the debtor in property... that is voidable under *applicable law* by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.¹⁵

Again, "applicable law" is interpreted to include state law causes of action, such as here where the Debtor's claim for relief is based upon an application of CUFTA. As the analysis above reveals, in order for the Debtor to assert a timely claim to recover alleged fraudulent transfers, it must rely on CUFTA's longer statute of limitations because the limitations period in section 548 of the Code has expired.

In asserting its sovereign immunity defense, the Defendant does not dispute that section 106 abrogates sovereign immunity with respect to section 544 of the Code; however, the Defendant denies that section 106 abrogates sovereign immunity with respect to actions brought under 544(b)(1), which are predicated on state law. In other words, the Defendant argues that if sovereign immunity prohibits an unsecured creditor from bringing a non-bankruptcy state law claim against the Defendant, then sovereign immunity similarly prohibits a trustee who steps into the shoes of an unsecured creditor from bringing the same non-bankruptcy state law claim under

¹³ C.R.S.A. § 38-8-110.

¹⁴ 11 U.S.C. § 106.

¹⁵ 11 U.S.C. § 544(b)(1) (emphasis added).

section 544(b)(1). The Court disagrees and finds that the abrogation of sovereign immunity extends to all sections of 544, regardless of whether the application of 544(b)(1) is predicated on a state law cause of action such as CUFTA, or, for that matter, any other “applicable law.”

Following the United States Supreme Court’s decision in *Central Virginia Community College v. Katz*, there is no longer a genuine dispute as to the validity of Congress’ waiver of sovereign immunity with respect to the Bankruptcy Code sections listed in section 106(a).¹⁶ With regard to section 544, in particular, Congress chose to explicitly waive sovereign immunity with respect to the entirety of section 544.¹⁷ In drafting section 106(a), Congress did not carve out section 544(b)(1) from this waiver. If Congress intended to retain a sovereign immunity defense to actions brought under section 544(b)(1), Congress certainly could have done so. This Court refuses to read into section 106(a) an exclusion to the waiver of sovereign immunity which Congress did not specifically provide. To do so would be improper and result in a judicially created amendment to an otherwise clear and unambiguous statute.¹⁸ Thus, the Court agrees with numerous other courts which have decided this same issue that “[b]y including section 544 in the list of Bankruptcy Code sections set forth in section 106(a), Congress knowingly included state law causes of action within the category of suits to which a sovereign immunity defense could no longer be asserted.”¹⁹ Thus, the Plaintiff’s claim under section 544(b)(1) is not barred by sovereign immunity and the Defendant’s Motion for Summary Judgment on this issue is denied.

d. Action to Recover A Fraudulent Transfer Does Not Require An Administrative Claim for A Refund under Internal Revenue Code § 7422

The Defendant argues that Internal Revenue Code (I.R.C.) section 7422 preempts the Plaintiff’s claim under CUFTA and mandates that the Plaintiff must file an administrative claim for a tax refund before it may pursue any other cause of action for recovery from the IRS. In addition, the Defendant argues that the IRC’s two-year statute of limitations for refund claims strongly indicates that Congress would not have allowed a four-year or longer time frame for recovery of claims under Bankruptcy Code section 544(b). The Court finds the Defendant’s argument unpersuasive and that I.R.C. section 7422 is completely inapplicable to the facts at hand.

First, in advancing its argument for I.R.C. section 7422 to preempt CUFTA, the Defendant continues to confuse the Plaintiff’s claim under section 544(b)(1) of the Bankruptcy Code for a claim which is merely brought under state law. The fact of the matter is that the

¹⁶ See *Central Virginia Community College v. Katz*, 546 U.S. 356, 126 S.Ct. 990, 163 L.Ed. 2d 945 (2006); see also 2 Collier on Bankruptcy ¶ 106.02[2][b] (Alan N. Resnick & Henry J. Somme reds., 16th ed.) (“The constitutionality of the Bankruptcy Code sections listed in section 106(a) is not in doubt[.]”).

¹⁷ 11 U.S.C. § 106(a).

¹⁸ *In re Equipment Acquisition Resources, Inc.*, 485 B.R. 586, 593 (N.D.Ill. 2013).

¹⁹ *In re C.F. Foods, L.P.*, 265 B.R. 71, 85 (Bankr.E.D.Pa. 2001); see also *In re Equipment Acquisition Resources, Inc.*, 485 B.R. 586 (N.D.Ill. 2013); *In re DBSI, Inc.*, 463 B.R. 709 (Bankr.D.Del. 2012); *In re Pharmacy Distrib. Servs., Inc.*, 455 B.R. 817 (Bankr.S.D.Fla. 2011).

Plaintiff has asserted a federal cause of action, provided for pursuant to section 544(b)(1) of the Bankruptcy Code, which is merely predicated on what could have happened under state law prior to bankruptcy. The Plaintiff's claim is not a bare state law claim asserted in a state court. In fact, absent section 544(b)(1) of the Bankruptcy Code, the Plaintiff would have no claim at all. The Plaintiff's claim is one which is provided for under federal law in an area where Congress has the exclusive authority to draft legislation under Article I, Section 8 of the United States Constitution. Thus, the Defendant's argument for federal preclusion of the Plaintiff's state law cause of action is based on the false premise that the Plaintiff has asserted a state law cause of action. The Plaintiff has asserted a federal cause of action and summary judgment in favor of the Defendant on the basis of preemption is inappropriate.

Second, not only is I.R.C. section 7422 not preclusive, it is entirely inapplicable to the facts at hand. I.R.C. section 7422 states, in relevant part:

No suit or proceeding shall be maintained in any court for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Secretary, according to the provisions of law in that regard...[.]²⁰

Under its express terms, I.R.C. section 7422 is applicable when taxes have been improperly assessed or are not otherwise properly due. Such is not the case here. In this case, the Plaintiff does not allege that the taxes due to be paid by Lochmiller were erroneously or illegally assessed or collected, or excessive or wrongfully collected. Rather, the allegations which give rise to the Plaintiff's cause of action state that Lochmiller used the Debtor's funds to pay his own income taxes and the Debtor received no value in return for this transfer. These allegations give rise to an entirely different cause of action than allegations which would invoke the application of I.R.C. section 7422. The Debtor seeks a money judgment under section 544 and 550 of the Bankruptcy Code for the recovery of funds fraudulently transferred from the Debtor to the Defendant. As the United States Bankruptcy Court for the Eastern District of California explained in response to an identical argument advanced by the IRS under similar circumstances:

[I]n pursuing the present claims against the IRS, the trustee is not standing in the shoes of the debtors, as taxpayers, seeking to recover tax refunds, but rather, in the shoes of a creditor seeking to recover property fraudulently transferred, within the meaning of [state fraudulent transfer law], or the value of such property.²¹

This Court agrees with the above bankruptcy court's apt description. In short, the facts before this Court are completely inapplicable to a refund analysis under I.R.C. section 7422.

²⁰ 26 U.S.C. § 7422(a).

²¹ *Sharp v. United States (In re SK Foods, L.P.)*, 2010 WL 6896448 (Bankr.E.D.Cal. July 14, 2010); *see also Furr v. United States (In re Pharmacy Distrib. Servs., Inc.)*, 455 B.R. 817, 822 (Bankr.S.D.Fla. 2010).

Likewise, any statute of limitations for refund claims has no application to the Court's understanding of Bankruptcy Code sections 544 and 106 and those sections implications for sovereign immunity and time limits for bringing claims. As discussed above, sections 544 and 106 are clear and unambiguous, therefore, it is improper for the Court to speculate on the intention of Congress with regard to refund claims when such an inquiry is unnecessary to the Court's understanding of Bankruptcy Code sections 544 and 106.

In short, I.R.C. section 7422 simply has no bearing on this Court's interpretation of Bankruptcy Code sections 544 and 106, nor does I.R.C. preempt the Plaintiff's action in any way. Thus, the Court declines to grant the Defendant's Motion for Summary Judgment on these grounds.

e. Good Faith and Reasonably Equivalent Value Are Questions of Fact and Those Facts Are Disputed

The Defendant seeks to retain the transfers in question by asserting the defense that it is a subsequent transferee which took the transfers at issue in good faith and for reasonably equivalent value. Good faith and reasonably equivalent value are factual determinations which are based on the totality of the circumstances and available evidence.²² Such issues are rarely decided on summary judgment and given the disputed material facts here, the Court finds this case to be no exception.

In addition, there is a genuine and material dispute as to the Defendant's self-proclaimed status as a subsequent transferee. In many circuits, including the Tenth Circuit, an initial transferee is one who exercises dominion and control over the money which has been transferred.²³ Similar to questions of good faith and reasonably equivalent value, questions of dominion and control are inherently factual. In order to determine these issues, the Court must hear testimony and receive evidence at trial. Therefore, the Court denies the Defendant's Motion for Summary Judgment on the basis of good faith, reasonably equivalent value and status as a subsequent transferee.

²² *Jobin v. Resolution Trust Corp.*, 160 B.R. 161, 169 (D.Colo. 1993) ("Whether a transfer is made for reasonably equivalent value is a question of fact to be determined from all the evidence in a particular case."); *In re Independent Clearing House Co.*, 77 B.R. 843, 862 (D.Utah 1987) (remanding to bankruptcy court for factual findings on question of whether defendants took payments in good faith).

²³ *Malloy v. Citizens Bank of Sapulpa (In re First Sec. Mortgage Co.)*, 33 F.3d 42, 43-44 (10th Cir. 1994).

IV. CONCLUSION AND ORDER

For the reasons stated herein,

IT IS THEREFORE ORDERED that the Defendant's Motion for Summary Judgment on the Debtor's claims brought under section 548 of the Code is GRANTED.

IT IS FURTHER ORDERED that the Defendant's Motion for Summary Judgment on the Debtor's claims brought under section 544 of the Code is DENIED.

Dated this 18th day of September, 2013.

BY THE COURT:



Sidney B. Brooks,
United States Bankruptcy Judge